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The Iran-Libya Sanctions Act (ILSA)

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Summary

The Iran-Libya Sanctions Act (ILSA, P.L. 104-172) was due to expire on August 5, 2001, 5 years after enactment. Debate on renewal of ILSA centered on the difficulties incurred in implementing it, reactions to ILSA on the part of U.S. allies, and changes in U.S. relations with Iran and Libya since enactment. On August 3, 2002, President Bush signed into law H.R. 1954, P.L. 107-24, the ILSA Extension Act of 2001, renewing ILSA for another 5 years. No firms have been sanctioned under ILSA. This report will be updated to reflect legislative developments. See also CRS Issue Brief IB93033, *Iran: Current Developments and U.S. Policy*, and CRS Issue Brief IB93109, *Libya*.

Background and Passage of ILSA

ILSA was conceived in the context of a tightening of U.S. sanctions on Iran during the first term of the Clinton Administration. Most experts attributed the imposition of additional sanctions to Iran's stepped up efforts to acquire nuclear expertise — it signed a contract with Russia in January 1995 for construction of a nuclear power reactor at Bushehr — and to a 1994-1995 spate of terrorist attacks in Israel by the Islamist organizations Hamas and Palestine Islamic Jihad, both of which receive some financial and material assistance from Iran, according to annual U.S. State Department reports on international terrorism. In 1995, President Clinton issued two executive orders, including Executive Order 12957 (March 15, 1995), which banned U.S. investment in Iran's energy sector, and Executive Order 12959 (May 6, 1995), which banned U.S. trade with and investment in that country.

The Clinton Administration and many in Congress maintained that the new U.S. sanctions might deprive Iran of the ability to acquire weapons of mass destruction (WMD) and fund terrorist groups by hindering its ability to modernize its key source of revenue — the petroleum sector. The effect on Iran would be significant, according to this view, if U.S. allies joined the U.S. trade and investment ban. Oil revenues account for about 10% of Iran's GDP. Iran's onshore oil fields, as well as its oil industry infrastructure, were old and needed substantial modernization and investment, and its large natural gas resources (believed second largest in the world, after Russia) were not developed at all.

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Iranian officials were predicting that, without substantial new investment, Iran might become a net *importer* of oil by 2010.

When U.S. allies refused to adopt similar sanctions, the Clinton Administration and Congress believed that it might be necessary for the United States to try to deter foreign countries from undermining the U.S. effort against Iran. Iran provided the United States an apparent opportunity when it launched its first major effort to open its energy sector to foreign investment. Iran had banned this investment after the November 1979 Islamic revolution on the grounds that foreign firms would gain undue control or influence over Iran's resources. To accommodate that philosophy, while recognizing that its economy was in jeopardy without foreign help, Iran developed a "buy-back" investment program. Under that plan, foreign firms recoup their investments from the proceeds of oil and gas discoveries; they do not receive equity positions. Throughout 1995, Iran advertised a major bidders' meeting in Tehran set for November 11-14, 1995, at which Iran would provide details on ten major energy projects open to foreign investment.

In anticipation of Iran's bidders' meeting, some in Congress, with input from the Clinton Administration, developed legislation to sanction foreign firms that assist Iran's energy sector. On September 8, 1995, Senator D'Amato introduced the first version of what later became ILSA, the "Iran Foreign Oil Sanctions Act of 1995," which would impose sanctions on foreign firms' export to Iran of sophisticated energy hardware and technology. The bill passed the Senate on December 18, 1995 (voice vote) but, in contrast to the introduced version, imposed sanctions on foreign investment in Iran's energy sector. The alteration of the bill appeared to take into account Clinton Administration concerns that U.S. monitoring of foreign exports to Iran would be too difficult to implement. On December 20, 1995, the Senate passed still another version with an amendment, sponsored by Senator Kennedy, that applied all provisions to Libya as well as Iran. Observers widely interpreted the amendment as a response to efforts by the families of the victims of the December 21, 1988 downing of Pan Am 103 to pressure Libya to yield for trial the two suspects in the bombing, both allegedly agents of Libyan intelligence. The House passed its version of the bill, H.R. 3107, on June 19, 1996, by a vote of 415-0. The Senate passed a slightly different version on July 16, 1996 by unanimous consent. The House agreed to the Senate amendment and the President signed the bill into law (P.L. 104-172) on August 5, 1996.

Key ILSA Provisions

ILSA requires the President to impose at least two out of a menu of six sanctions on foreign companies that make an "investment" of more than \$20 million in one year in Iran's energy sector, or \$40 million in one year in Libya's energy sector. Prior to the suspension of U.N. sanctions against Libya, which was triggered by Libya's handover of the two Pan Am 103 suspects in April 1999, foreign firms were also subject to the sanctions if they export to Libya technology that can be used to develop its energy sector, to develop weapons of mass destruction (WMD), to enhance its conventional military, or to maintain its aviation capabilities (Section 5(b)(1)). These exports had been banned under Pan Am 103-related Security Council Resolutions 748 (March 31, 1992) and 883 (November 11, 1993). The six sanctions provided for in ILSA (Section 6) are the following:

- Denial of Export-Import Bank loans, credits, or credit guarantees for U.S. exports to the sanctioned firm.
- Denial of licenses for the U.S. export of military or militarily-useful technology to the sanctioned firm.
- Denial of U.S. bank loans exceeding \$10 million in one year to the sanctioned firm.
- If the sanctioned firm is a financial institution, a prohibition on that firm's service as a primary dealer in U.S. government bonds; and/or a prohibition on that firm's service as a repository for U.S. government funds. (Each counts as one sanction.)
- Prohibition on U.S. government procurement from the sanctioned firm.
- A restriction on imports from the sanctioned firm, in accordance with the International Emergency Economic Powers Act (50 U.S.C. 1701 and following).

Waiver/Expiration Provisions. There are two grounds on which the President may waive ILSA sanctions. Under Section 4(c), the President may waive sanctions if the parent country of the violating firm agrees to impose economic sanctions on Iran. This waiver provision does not apply to Libya. Under Section 9(c) of the law, the President may waive sanctions on the grounds that doing so is important to the U.S. national interest. This waiver applies to Iran and Libya. ILSA terminates for Iran if Iran ceases its efforts to acquire WMD and is removed from the U.S. list of state sponsors of terrorism. For Libya, ILSA terminates if the President determines that Libya has fulfilled the requirements of all U.N. resolutions relating to the attack on Pan Am 103. (On January 31, 2001, one of the Libyan suspects, Abd al-Baset al-Magrahi, was convicted of the bombing. Libya has not yet fulfilled the requirement to accept responsibility and compensate the families of the victims, although press reports since early 2003 have said Libya is close to taking these steps.)¹ Even if none of these conditions were met, ILSA was to sunset on August 5, 2001 (5 years after enactment).

ILSA Renewal

In the runup to ILSA's expiration, Congress debated renewal of the law in the context of a somewhat improved climate in U.S. relations with both Iran and Libya. In its last two years, the Clinton Administration eased sanctions on Iran in response to the ascendancy of a more moderate government, led by President Mohammad Khatemi, and on Libya in response to the yielding for trial of the Libyan suspects in Pan Am 103. Some believe the changed climate reduced the need for ILSA, which critics argue has hindered rather than promoted multilateral coordination on Iran and Libya policy. Proponents of renewal maintained that not only had ILSA accomplished some of its key objectives but that both Iran and Libya would view ILSA's expiration as a concession, reducing their incentive to adopt policies the United States favors.

¹ For further information on Libya, see CRS Issue Brief IB93109, *Libya*, by Clyde R. Mark.

A House bill, H.R. 1954, was reported to the full House by the International Relations Committee on June 20, 2001, by a vote of 41 to 3. A proposed amendment to renew the law for only 2 years, which was supported by the Bush Administration on the grounds that a review after 2 years allows greater flexibility than a 5-year renewal, was defeated by a vote of 34 to 9. The bill modified ILSA by incorporating an amendment that would lower the investment trigger for Libya to \$20 million in one year, the same as for Iran, and changed the definition of investment to treat any additions to pre-existing investment as a new contract. This appeared intended to encompass much of the foreign investment taking place in Libya's energy sector, where foreign companies had been operating long before ILSA was enacted. The final version of H.R. 1954, passed by the House on July 26, 2001, by a vote of 409-6, and by the Senate the following day by unanimous consent, required an Administration report on ILSA's effectiveness within 24-30 months (as early as August 2003). President Bush signed H.R. 1954 on August 3, 2002 (P.L. 107-24).

Implementation and Effectiveness of ILSA

ILSA, particularly when first enacted, provoked vocal opposition from U.S. allies, especially those in the European Union (EU). Traditionally skeptical of economic sanctions as a policy tool, the EU states took exception to ILSA as an extraterritorial application of U.S. law. Some EU states criticized ILSA as a "double standard" in U.S. foreign policy, in which the United States worked against the Arab League boycott of Israel while at the same time promoted a worldwide boycott of Iran. The EU countries threatened formal counter-action in the World Trade Organization (WTO).

The Clinton Administration asserted that the rationale for ILSA remained sound, but it also sought to balance implementation with the need to defuse a potential trade dispute with the EU. In April 1997, the United States and the EU formally agreed to try to avoid a trade confrontation over ILSA and the "Helms-Burton" Cuba sanctions law (P.L. 104-114). The agreement contributed to a decision by the Clinton Administration to waive ILSA sanctions on the first project determined to be in violation: a \$2 billion² contract (signed in September 1997) for Total SA of France and its minority partners, Gazprom of Russia and Petronas of Malaysia to develop phases 2 and 3 of the 25-phase South Pars gas field. The Administration announced the waiver on May 18, 1998, citing national interest grounds (Section 9(c) of ILSA), after the EU pledged to increase cooperation with the United States on non-proliferation and counter-terrorism. The announcement indicated that EU firms would likely receive waivers for future projects that were similar.

The Bush Administration has indicated it is adopting the same policy on ILSA as the Clinton Administration, preferring, as did the Clinton Administration, to try to work cooperatively with the EU to curb Iran's nuclear program and limit its support for international terrorism. According to the Bush Administration, ILSA has not stopped energy sector investment, although some say the law slowed Iran's energy development,

² Dollar figures for energy investment contracts with Iran represent public estimates of the amounts investing firms are expected to spend during the life of the project, which might in some cases be several decades.

and Iran's sustainable oil production has not increased significantly since the early 1990s, despite the new investment.³

Since the South Pars case, several projects — all involving Iran, not Libya — have been formally placed under review for ILSA sanctions, but no additional sanctions determinations were announced by the Clinton Administration, or subsequently by the Bush Administration.⁴ Recent energy sector investment in Iran includes the following, and work has begun on all but the most recent of the agreements:

- A February 1999 award to France's Elf Aquitaine (now merged with Totalfina) and Italy's ENI to develop the Doroud oil field. The estimated value of the investment is \$1 billion.
- A project, run by Elf Aquitaine and Canada's Bow Valley, to develop the Balal oil field. The project had foundered for lack of financing until Elf's decision to join it in April 1999. The estimated value is \$300 million.
- A November 1999 contract for Royal Dutch/Shell (U.K. and the Netherlands) to develop the Soroush and Nowruz oil fields. The estimated value is \$800 million.
- A July 2000 award to ENI to develop phases 4 and 5 of South Pars. The estimated value is \$3.8 billion.
- An exploration contract for Norway's Norsk Hydro to develop the Anaran oil field, signed in April 2000. The estimated value is unknown.
- In January 2001 a U.K. firm, Enterprise Oil, took a 20% stake in phases 6, 7, and 8 of South Pars.
- In March 2001, Iran announced it had signed a \$226 million contract for a consortium led by Sweden's GVA Consultants to explore for oil in Iran's portion of the Caspian Sea.
- On June 30, 2001, ENI signed a deal, estimated to be worth \$550 million to \$1 billion, to develop Iran's Darkhovin oil field.

³ Testimony of Deputy Assistant Secretary of State Anna Borg before the House International Relations Committee, Subcommittee on the Middle East and Central Asia. June 17, 2003.

⁴ The Clinton Administration began informal reviews of several projects in Libya, but U.S. officials say that foreign investment in Libya is more difficult to assess because Libya has consistently hosted foreign energy firms; projects there mostly represent continuations of investments made prior to ILSA's enactment. One such project is a \$5.5 billion gas pipeline from Libya to Sicily sponsored by Italy's ENI/Agip Gas. Other Libya projects appeared to fall under the trigger investment threshold. One project that has attracted congressional attention is a reported effort by a German firm, Wintershall, to acquire exploration rights in Libyan fields owned by U.S. firms.

- In December 2001, Japan and Iran reached agreement that a Japanese consortium would have first rights to negotiate to develop the large Azadegan field, an investment worth about \$2.8 billion. The two sides did not reach agreement by the target date of June 30, 2003, leaving Japan's status in the deal unclear. The government of Japan reportedly sought to link the deal to Iran's cooperation with the international community on intrusive inspections of its nuclear facilities.
- In May 2002, Canada's Sheer Energy took a 49% stake in an \$88 million project to develop the Masjid-e-Soleyman onshore oil field.
- In September 2002, South Korea's LG Engineering Group, in partnership with two Iranian firms, was given a \$1.6 billion stake in phases 9 and 10 of South Pars.
- In October 2002, the Norwegian firm Statoil signed an agreement to invest \$300 million in phases 6, 7, and 8 of South Pars.

Energy Routes Transiting Iran. ILSA's provisions and its definition of "investment" do not specifically mention the development of energy transit routes through Iran as sanctionable activity. The Clinton Administration position was that, under certain conditions, the construction of such routes might constitute sanctionable investment and would be reviewed under ILSA. According to many observers, the Clinton Administration adopted that position in order to promote a new Central Asian/Caspian energy route from Azerbaijan (Baku) to Turkey (Ceyhan) that would bypass Iran and Russia. This would have the effect of denying Iran the benefit of transit fees and political and economic leverage over Western energy supplies. The Bush Administration has not announced any alteration of this stance. Construction of this pipeline has begun and the first section was been laid in Azerbaijan in July 2003.

At the same time, the United States has responded to the needs of a key regional ally, Turkey, for energy supplies. A few weeks after ILSA was enacted, Turkey and Iran reached final agreement on a plan to construct a natural gas pipeline from Iran to Turkey, with each country constructing the pipeline on its side of their common border. Turkey later announced that, at least initially, it would import gas from Turkmenistan through this new pipeline. In July 1997, the State Department said that the project did not qualify for ILSA sanctions because Turkey would be importing gas from Turkmenistan, not Iran, and the project would therefore not benefit Iran's energy sector directly. Others believe that, whether or not Iranian energy would be purchased under this project, construction of energy routes alone would not meet the definition of investment in Section 14 of ILSA.⁵ Iranian gas exports to Turkey began in 2001, in apparent contravention of Turkey's pledges to the United States that it would not buy Iranian gas directly.

⁵ ILSA defines "investment" as the entry into a contract that includes responsibility for the development of petroleum resources in Iran or Libya; the purchase of a share of ownership in that development; and participation in royalties, earnings, or profits from the development. ILSA states that the term investment does not include contracts or the financing of contracts to sell goods, services, or technology to Iran's energy sector.